

File No. **100315**

Committee Item No. **6**
Board Item No. 4

COMMITTEE/BOARD OF SUPERVISORS
AGENDA PACKET CONTENTS LIST

Sub - Committee: Budget and Finance

Date: April 21, 2010

Board of Supervisors Meeting

Date: 4/27/10

Cmte Board

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| <input type="checkbox"/> | <input type="checkbox"/> | MOU |
| <input type="checkbox"/> | <input type="checkbox"/> | Grant Information Form |
| <input type="checkbox"/> | <input type="checkbox"/> | Grant Budget |
| <input type="checkbox"/> | <input type="checkbox"/> | Subcontract Budget |
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| <input type="checkbox"/> | <input type="checkbox"/> | Award Letter |
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Completed by: Andrea S. Ausberry

Date Friday, April 16, 2010

Completed by: AA

Date 4/22/10

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10/10/10

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1 [Airport Concession Lease – Terminal 2 Specialty Store with Charles Chocolates, Inc.]

2
3 **Resolution approving the Terminal 2 Specialty Store Lease between Charles**
4 **Chocolates, Inc. and the City and County of San Francisco, acting by and through its**
5 **Airport Commission.**

6
7 WHEREAS, The Airport Commission has requested for proposals for the Terminal 2
8 Specialty Store Lease; and

9 WHEREAS, Charles Chocolates, Inc. was the highest ranked, responsive and
10 responsible proposer; and,

11 WHEREAS, The Airport Commission approved Resolution No. 10-0042, adopted
12 February 18, 2010, awarding the Terminal 2 Specialty Store Lease to Charles Chocolates,
13 Inc. now, therefore, be it

14 RESOLVED, That the Board of Supervisors hereby approves award of the Terminal 2
15 Specialty Store Lease No. 10-0042 to Charles Chocolates, Inc., copies of which are contained
16 in Board of Supervisors' File No. 100315.

Items 5, 6, 7, and 8
Files 10-0310, 10-0315, 10-0321, and 10-0322

Department(s):
San Francisco Airport (Airport)

EXECUTIVE SUMMARY

Legislative Objective

- File No. 10-0310: The proposed resolution would approve a Terminal 2 Book Store Lease between the City and County of San Francisco, acting on behalf of the San Francisco Airport (Airport) and Books Inc. for 2,994 square feet of space.
- File No. 10-0315: The proposed resolution would approve a Terminal 2 Specialty Store Lease between the Airport and Charles Chocolate, LLC for 928 square feet of space.
- File No. 10-0321: The proposed resolution would approve a Terminal 2 and Terminal 3 Electronic and Technology Lease between the Airport and Edge 1 Cellular, L.P. for 1,350 square feet of space.
- File No. 10-0322: The proposed resolution would approve a Terminal 2 and Terminal 3 Spa Lease between the Airport and XpresSpa SF International, Inc. for 2,031 square feet of space.

Key Points

- Based on a competitive Request for Proposal process, the Airport has recommended the award of four leases for retail services in its new domestic terminal, Terminal 2 (File Nos. 10-0310, 10-0315, 10-0321 and 10-0322), scheduled to open on January 1, 2011 and in its existing domestic terminal, Terminal 3 (File Nos. 10-0321 and 10-0322), which includes a (1) a bookstore (File No. 10-0310), (2) a specialty store (File No. 10-0315), (3) two electronic and technology stores in Terminals 2 and 3 (File No. 10-0321), and (4) two spas in Terminals 2 and 3 (File No. 10-0322).
- Three of the four proposed leases (Charles Chocolate, LLC, Edge 1 Cellular, L.P., and XpresSpa SF) are seven year leases, from January 1, 2011 through December 31, 2017. The Books Inc. lease is for 10-years, from January 1, 2011 through December 31, 2020.

Fiscal Impact

- Under the proposed four leases, the lessees would pay the Airport an annual rent of either the greater of (a) its percentage of gross revenues sales, or (b) the Minimum Annual Guarantee (MAG). The MAG was a competitive bid item. The estimated rent for the first year payable to the Airport under the proposed four leases would be \$1,011,000.
- In addition to the annual rent, under the proposed four leases, the lessees are required to pay the Airport annually a Tenant Infrastructure Fee and a Promotional Program Fee. The total annual Fees of \$7,634 for the first year payable to the Airport include \$331 in Tenant Infrastructure/Food Court Fees and \$7,303 in Promotional Program Fees
- The estimated rent and fees payable to the Airport for the first year of the proposed leases is \$1,018,634 (\$1,011,000 plus \$7,634).
- In addition, the four lessees are required to make one-time tenant improvements, at no cost to the Airport, at a minimum cost of \$2,556,050 for all four leases.

Recommendations

- Approve the proposed resolutions.

BACKGROUND/MANDATE STATEMENT

Background

Since 1954, Terminal 2 at the San Francisco Airport (Airport) operated as the International Terminal. Due to an increase in both domestic and international passenger traffic, the Airport constructed a new International Terminal in 2000, and in the fall of 2000 closed Terminal 2 to be renovated into a new domestic terminal. Renovations of Terminal 2 began in September 2008 and Terminal 2 is projected to be opened to domestic passengers in January 2011. Terminal 2 will have approximately 29,211 square feet of food and beverages and retail establishments.

The proposed four retail leases include a total of 7,303 square feet (see Table 2 below), which includes 5,654 square feet in the new Terminal 2 and 1,649 square feet in the existing Terminal 3 domestic terminal. Out of the total of 29,211 square feet to be leased in the new Terminal 2, the Airport awarded eight food and beverages leases¹ totaling 16,110 square feet, which were recommended by the Budget and Finance Subcommittee to the full Board of Supervisors on April 15, 2010. Those eight leases are subject to Board of Supervisors approval on April 20, 2010. Retail leases for the balance of the 7,447 square feet in Terminal 2 (29,211 less 5,654 for the proposed subject leases less 16,110) either (a) do not require Board of Supervisors approval² or (b) will be submitted to the Board of Supervisors in future legislation, as required.

On October 22, 2009, the Airport issued a Request for Proposal (RFP) for concession leases for both food and beverage spaces in Terminal 2 and retail spaces in Terminal 2 and Terminal 3. The proposed resolutions would approve four retail leases.

After advertising on the Airport's website, the Airport news publication, press releases, and local newspapers for the proposed four retail leases, the Airport received 13 proposals on January 6, 2010, which included (a) two bookstore proposals, (b) seven specialty store proposals, (c) three electronic and technology proposals, and (d) one spa proposal. The Airport Evaluation Committee³ evaluated and scored the written proposals for 11 firms⁴.

¹ The eight food and beverage leases include (a) one sit-down restaurant lease to D-Lew Enterprises (File No. 10-0317), (b) one gourmet market and wine bar lease to D-Lew Enterprises (File No. 10-0312), (c) one cocktail lounge lease to HBF Soto JV (File No. 10-0314), (d) one coffee and bakery lease to Gotham Enterprises (File No. 10-0318), and (e) four quick serve (facilities that prepare food as ordered) leases to HBF Soto JV (File No. 10-0320), BJ Annex (File No. 10-0313), Andale Management Group (File No. 10-0319), and Sankaku (File No. 10-0316)

² The following three leases do not require Board of Supervisors approval because such leases do not exceed ten years and/or have anticipated revenues of \$1,000,000 or greater: (a) one Regional Gift Store lease between the Airport and Avila Retail Development & Management, Inc., (b) one Museum Store lease between the Airport and Avila Retail Development & Management, Inc and (c) one Travel Store lease between the Airport and RDG Concessions.

³ The Airport Evaluation Committee consisted of five business and education leaders approved by the Airport Director.

⁴ Of the 13 proposals, two specialty store proposals (Hudson Group and the Paradise Shops) were not scored because the Airport ultimately separated the leases for the newspaper spaces from the specialty spaces, issuing a separate Newsstand RFP. Hudson Group and the Paradise Shops were only interested in developing specialty space, if they were also awarded the newsstand space.

In February of 2010, based on the Airport's RFP process, the Airport recommended the award of four separate retail leases to the following firms that received the highest score in each category (except for the specialty store lease, which was awarded to the second highest bidder⁵).

- (a) one bookstore lease to Books Inc. (File No. 10-0310),
- (b) one specialty store lease to Charles Chocolate, LLC (File No. 10-0315),
- (c) one electronic and technology store lease to Edge 1 Cellular, L.P., which includes two stores in Terminal 2 and Terminal 3 (File No. 10-0321), and
- (d) one spa lease to XpresSpa SF International, Inc., which includes two stores in Terminal 2 and Terminal 3 (File No. 10-0322).

The scores of these written proposals are shown in Table 1 below based on data provided by the Airport. The written proposal scores were based on the retail store firms' (a) proposed concept (30 points), (b) design intention and proposed capital investment (20 points), (c) business plan (20 points), (d) customer service and quality control (20 points), and (e) proposed MAG (10 points). The winning scores are listed as No. 1 in each of the four categories as shown in Table 1 below.

Table 1: Proposals for Terminal 2 Retail Leases

Bidders	Written Proposal Score	MAG
Total Possible Score	100	
BOOKSTORE		
1. Books Inc. as Compass Books, Inc.	90.92	\$200,000
2. Hudson Group as Hudson Books	83.60	\$210,000
SPECIALTY STORE		
1. Pacific Gateway Concessions, LLC as Destination Green	84.58	\$135,000
2. Charles Chocolate, LLC as Charles Chocolate*	76.34	\$145,000
3. RDG Concessions, LLC as Face Time	74.00	\$224,334
4. Avila Retail Development & Management, LLC. As Earth Spirit	73.62	\$135,000
5. Swatch Group, Inc. as Swatch	58.02	\$135,000
ELECTRONIC AND TECHNOLOGY STORE**		
1. Edge 1 Cellular, L.P. as I-Tech Experience	86.24	\$338,980
2. Bluwire SFO and JV Partners, LLC as BluWire	78.81	\$300,000
3a. Project Horizon as Project Horizon Sound Balance	72.93	\$285,000
3b. Project Horizon as Project Horizon Blackberry	69.61	\$285,000
SPA		
1. XpresSpa SF International, Inc. as XpresSpa***	82.96	\$250,000

Source: Airport

* Winning bidder

** There are only three Electronic and Technology proposals. Project Horizon submitted two Electronic and Technology plans under one proposal.

*** Only proposal submitted

⁵ The Airport initially awarded the specialty store lease to the highest scored bidder, Pacific Gateway Concessions (PGC). However, PGC declined the specialty store lease because firms were only allowed to win two leases in Terminal 2 and PGC already partnered with HBF-Soto for a cocktail lounge lease and a quick serve lease. Therefore, the Airport awarded the specialty store lease to the second highest bidder, Charles Chocolates, LLC.

Mandate Statement

In accordance with Charter Section 9.118(c), any lease exceeding ten years and/or having anticipated revenues of \$1,000,000 or greater is subject to Board of Supervisors approval.

DETAILS OF PROPOSED LEGISLATION

The proposed resolutions would authorize the Airport to enter into four separate retail space leases with four lessees for use of a total of 7,303 square feet including 5,654 square feet in Terminal 2 and 1,649 square feet in Terminal 3, as shown in Table 2 below. The Attachment provided by Mr. John Reeb, Senior Principal Property Manager of the Airport, shows the locations of the four retail lessees in Terminals 2 and 3.

Table 2: Square Foot of Terminal 2 Retail Leases

	Terminal 2 Square Feet	Terminal 3 Square Feet	Total Square Feet
BOOKSTORE			
Books Inc. as Compass Books, Inc.	2,994		2,994
SPECIALTY STORE			
Charles Chocolate, LLC as Charles Chocolate	928		928
ELECTRONIC AND TECHNOLOGY STORE			
Edge 1 Cellular, L.P. as I-Tech Experience	723	627	1,350
SPA			
XpresSpa SF International, Inc. as XpresSpa	1,009	1,022	2,031
Total	5,654	1,649	7,303

Source: Airport

Lease Term Period: Three of the proposed four leases will have a term of seven years from January 1, 2011 through December 31, 2017, as follows: (a) Charles Chocolate, LLC (Specialty Store lease), (b) Edge 1 Cellular, L.P. (Electronic and Technology Store Lease), and (c) XpresSpa SF International, Inc. (Spa Lease). The bookstore lease between the Airport and Books Inc. will have a term of ten years from January 1, 2011 through December 31, 2020. According to Mr. Reeb, Books Inc. will have a ten year lease because the bookstore will incur significantly greater tenant improvement expenditures than the other three tenants.

Mr. Reeb advises that the proposed four leases are consistent with the Airport's existing retail leases in Terminals 1 and 3.

Annual Rent: The proposed four leases would pay the Airport an annual rent of either the greater of (a) a percentage of gross sales, or (b) the Minimum Annual Guarantee (MAG), as shown in Table 3 below. The MAG is subject to an annual Consumer Price Index (CPI)⁶ adjustment on the anniversary date of the proposed leases. If the CPI decreases, the rent will not decrease to a value less than the previous year's rent under the provisions in the proposed leases.

⁶ The CPI represents changes in prices of all goods and services for All Urban Consumers in the San Francisco-Oakland-San Jose area and is published by the Bureau of Labor Statistics under the United States Department of Labor.

Table 3: Minimum Annual Guarantee (MAG) and Percentage of Gross Sales

	MAG	Percentage of Gross Sales
BOOKSTORE		
Books Inc. as Compass Books, Inc.	\$200,000	<ul style="list-style-type: none"> • 8% up to \$2,000,000 • 10% over \$2,000,000
SPECIALTY STORE		
Charles Chocolate, LLC as Charles Chocolate	\$145,000	<ul style="list-style-type: none"> • 12% up to \$500,000 • 14% from \$500,000.01 to \$1,000,000 • 16% over \$1,000,000
ELECTRONIC AND TECHNOLOGY STORE		
Edge 1 Cellular, L.P. as I-Tech Experience	\$338,980	<ul style="list-style-type: none"> • 12% up to \$500,000 • 14% from \$500,000.01 to \$1,000,000 • 16% over \$1,000,000
SPA		
XpresSpa SF International, Inc. as XpresSpa	\$250,000	<ul style="list-style-type: none"> • 12% up to \$2,500,000 • 14% over \$2,500,000
Total	\$933,980	

Source: Airport

As stated above, the bidders submitted a MAG as part of their competitive proposal. The percentage of gross sales rates were specified in the Request for Proposals (RFP), which according to Mr. Reeb, were based on the existing rent structures of retail stores in the Airport's Domestic Terminals 1 and 3, and also, based on the current retail market.

A description is shown below of the Airport's Promotional Program Fee and Tenant Infrastructure Fee

Promotional Program Fee: The Promotional Program Fee allows the Airport to recover a portion of the Airport's costs to advertise and promote the retail stores in Terminals 2 and 3. The four lessees are required to pay an annual rate of \$1.00 per square foot for the Promotional Program, for an annual total of \$7,303, as shown in Table 4 below. The Promotional Program Fee is subject to an annual CPI adjustment on the anniversary date of the proposed leases. If the CPI decreases, the fee will not decrease to a value less than the previous year's fee under the provisions in the proposed leases.

Table 4: Annual Promotional Program Fee

	Square Foot	Rate	Fee*
BOOKSTORE			
Books Inc. as Compass Books, Inc.	2,994	\$1.00	\$2,994
SPECIALTY STORE			
Charles Chocolate, LLC as Charles Chocolate	928	\$1.00	\$928
ELECTRONIC AND TECHNOLOGY STORE			
Edge 1 Cellular, L.P. as I-Tech Experience	1,350	\$1.00	\$1,350
SPA			
XpresSpa SF International, Inc. as XpresSpa	2,031	\$1.00	\$2,031
		Total	\$7,303

Source: Airport

* Fee for the first year of the lease.

Tenant Infrastructure Fee: The Tenant Infrastructure Fee allows the Airport to recover over the term of the lease a portion of the costs for the construction of the proposed retail spaces in Terminal 2⁷. According to Mr. Reeb, one lessee Charles Chocolate is not required to pay the Tenant Infrastructure Fee for their Specialty Store Lease because significant construction is not required. As shown in Table 5 below, the three other proposed leases would pay \$0.07 per square foot per year for their retail space in Terminal 2, for a total of \$330.82 per year. A Tenant Infrastructure Fee is not charged for the Terminal 3 spaces since the spaces in Terminal 3 have already been constructed. The Tenant Infrastructure Fee rate will remain the same throughout the term of the leases.

Table 5: Annual Tenant Infrastructure Annual Fee

	Square Foot in Terminal 2	Rate	Fee
BOOKSTORE			
Books Inc. as Compass Books, Inc.	2,994	\$0.07	\$209.58
ELECTRONIC AND TECHNOLOGY STORE			
Edge 1 Cellular, L.P. as I-Tech Experience	723	\$0.07	\$50.61
SPA			
XpresSpa SF International, Inc. as XpresSpa	1,009	\$0.07	\$70.63
		Total	\$330.82*

Source: Airport

* Rounded to \$331

Minimum Investment Amount: The four leases also require that the lessees refurbish, redecorate, and modernize the interiors and exteriors of their specific retail space, at no cost to the Airport, at a required rate of \$350 per square foot, with a total one-time tenant improvement amount of \$2,556,050, as shown in Table 6 below.

⁷ Tenant Infrastructure includes base building work, demolition of existing facilities, and development of lease space shell and core.

Table 6: Minimum Investment One-time Tenant Improvements Amount

	Square Foot	Rate	Fee
BOOKSTORE			
Books Inc. as Compass Books, Inc.	2,994	\$350	\$1,047,900
SPECIALTY STORE			
Charles Chocolate, LLC as Charles Chocolate	928	\$350	\$324,800
ELECTRONIC AND TECHNOLOGY STORE			
Edge 1 Cellular, L.P. as I-Tech Experience	1,350	\$350	\$472,500
SPA			
XpresSpa SF International, Inc. as XpresSpa	2,031	\$350	\$710,850
		Total	\$2,556,050

Source: Airport

FISCAL ANALYSIS

Projected Revenue of the Annual Terminal 2 Retail Leases Including Rent and Fees for the First Year of the Four Proposed Leases

The Airport is estimated to receive a total of \$1,018,634 in the first year from the four proposed leases, which includes \$1,011,000 from a combination of annual percentage of gross sales rent and MAG rent (see Table 7 below) and \$7,634 in Tenant Infrastructure and Program Promotion fees (see Table 8 below).

As shown in Table 7 below, Edge 1 Cellular, L.P. and XpresSpa SF International, Inc. are projected by the Airport to pay the annual percentage rent while Books Inc. and Charles Chocolate are projected to pay the MAG rent in the first year of the leases. If the MAG exceeds the annual percentage rents from gross sales in the first year, the Airport would be paid a total MAG of \$933,980 (see Table 3 above), or \$77,020 less (\$1,011,000 less \$933,980) than the estimated combination of MAG rent and percentage of gross sales rent of \$1,011,000, as shown in Table 7 below.

In addition, the four lessees will pay a required total of \$2,556,050 in one-time tenant improvements as shown in Table 6 above.

Table 7: Projected First Year Annual Rent of Terminal 2 Retail Leases

	MAG	Projected Sales	Projected Percentage Sales Rent			Total	Total Annual Rent Payments to the Airport
			8% of up to \$2,000,000	10% of over \$2,000,000.01	14% of \$500,000.01 up to \$1,000,000		
BOOKSTORE						Total	
Books Inc.	\$200,000	\$2,400,000	\$160,000	\$40,000		\$200,000	\$200,000
SPECIALTY STORE			12% of up to \$500,000	14% of \$500,000.01 up to \$1,000,000	16% of over \$1,000,000.01	Total	
Charles Chocolate, LLC	\$145,000	\$1,050,000	\$60,000	\$70,000	\$8,000	\$138,000	\$145,000
ELECTRONIC & TECHNOLOGY STORE			12% of up to \$500,000	14% of \$500,000.01 up to \$1,000,000	16% of over \$1,000,000.01	Total	
Edge 1 Cellular, L.P.	\$338,980	\$2,700,000	\$60,000	\$70,000	\$272,000	\$402,000	\$402,000
SPA			12% of up to \$2,500,000	14% of over \$2,500,000.01		Total	
XpresSpa SF International, Inc.	\$250,000	\$2,200,000	\$264,000			\$264,000	\$264,000
						Total	\$1,011,000

Source: Airport


Table 8: Projected First Year Fees of Terminal 2 Retail Leases

	Tenant Infrastructure	Promotional Program Fee	Total
BOOKSTORE			
Books Inc. as Compass Books, Inc.	\$209.58	\$2,994	\$3,204
SPECIALTY STORE			
Charles Chocolate, LLC as Charles Chocolate	--	\$928	\$928
ELECTRONIC & TECHNOLOGY STORE			
Edge 1 Cellular, L.P. as I-Tech Experience	\$50.61	\$1,350	\$1,401
SPA			
XpresSpa SF International, Inc. as XpresSpa	\$70.63	\$2,031	\$2,102
Total	\$330.82	\$7,303	\$7,634

Source: Airport

RECOMMENDATION

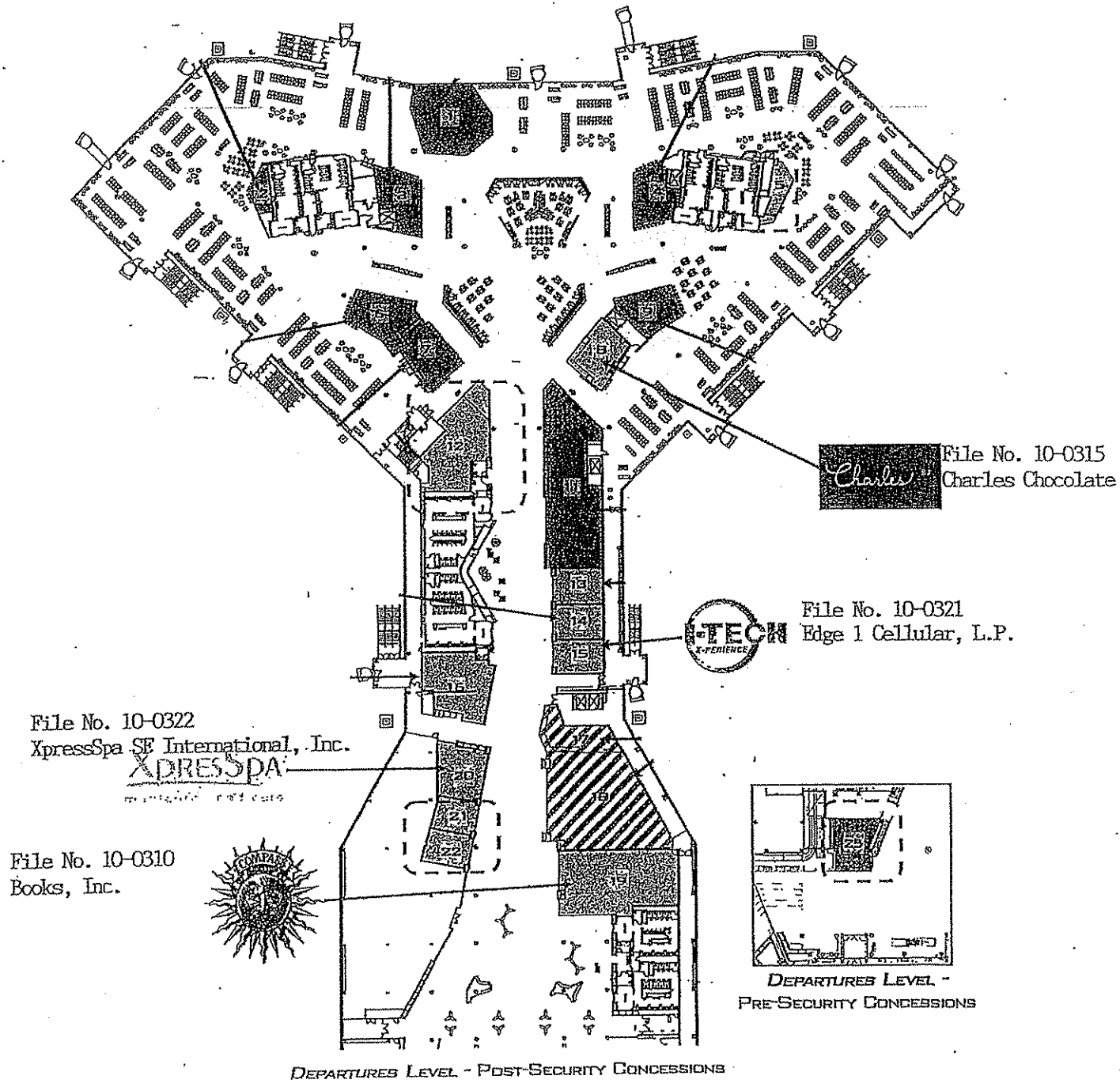
Approve the proposed resolutions.



Harvey M. Rose

cc: Supervisor Avalos
Supervisor Mirkarimi
Supervisor Elsbernd
President Chiu
Supervisor Alioto-Pier
Supervisor Campos
Supervisor Chu
Supervisor Daly
Supervisor Duffy
Supervisor Mar
Supervisor Maxwell
Clerk of the Board
Cheryl Adams
Controller
Greg Wagner

TERMINAL 2 CONCESSION PROGRAM



Re-issued

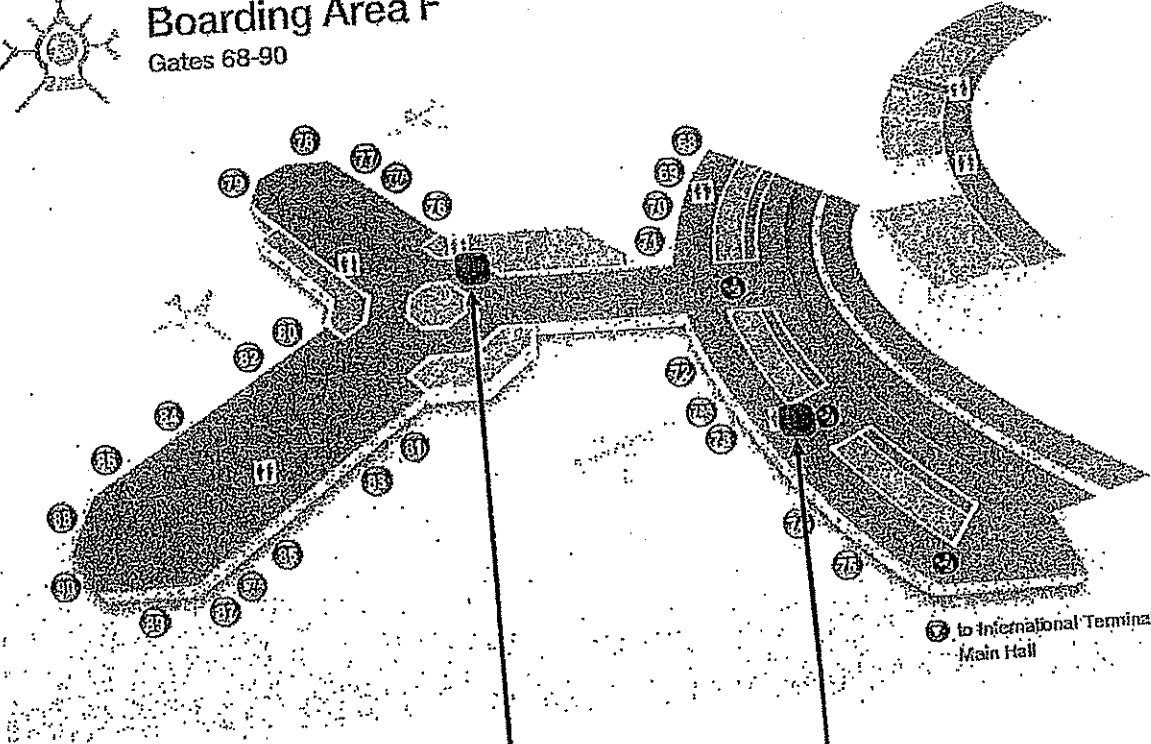
5,6,7&8 - 10

Terminal 3



Boarding Area F
Gates 68-90

to Boarding Area E



to International Terminal
Main Hall

XpressSpa

manicure pedicure

File No. 10-0322

XpressSpa SF International, Inc.



File No. 10-0321
Edge 1 Cellular, L.P.

LEASE AGREEMENT
FOR THE
TERMINAL 2 SPECIALTY STORE
AT SAN FRANCISCO INTERNATIONAL AIRPORT

by and between

CHARLES CHOCOLATES, INC.,
as tenant

and

CITY AND COUNTY OF SAN FRANCISCO
ACTING BY AND THROUGH ITS AIRPORT COMMISSION,
as landlord

Gavin Newsom
Mayor

AIRPORT COMMISSION

Hon. Larry Mazzola, President
Hon. Linda S. Crayton, Vice President
Hon. Caryl Ito
Hon. Eleanor Johns
Hon. Richard J. Guggenlime

John L. Martin
Airport Director

February 18, 2010

Lease No. 10-0042

See file # 100315 / a complete copy

5.	ASSIGNMENT OR SUBLETTING	
5.1	No Assignment.....	17
5.2	Changes in Tenant	17
5.3	No Release	17
5.4	Subleasing	17
5.5	Excess Rent.....	18
5.6	Acceptance of Rent.....	18
5.7	Waiver.....	18
6.	TAXES, ASSESSMENTS AND LIENS	
6.1	Taxes.....	18
6.2	Other Liens.....	19
7.	INVESTMENTS; ALTERATIONS	
7.1	City's Construction Obligation.....	19
7.2	Tenant's Work; Minimum Investment.....	19
7.3	City's Approval Rights	19
7.4	Structures and Fixtures	20
7.5	Notice and Permits	20
7.6	Title to Alterations	20
7.7	Effect of Alterations on Airport.....	21
7.8	[INTENTIONALLY DELETED]	
7.9	Labor Harmony.....	21
8.	UTILITIES	
8.1	Services Provided.....	22
8.2	Utility Costs	22
8.3	Shared Telecommunications Services	22
8.4	Waiver of Damages.....	22
9.	MAINTENANCE AND REPAIR	
9.1	"As-Is" Condition	22
9.2	Tenant's Maintenance Obligations	23
9.3	Tenant's Pest Management Obligation.....	23
10.	SIGNS AND ADVERTISING	
10.1	Signs and Advertising.....	24
10.2	Prohibition of Tobacco Sales and Advertising.....	24
10.3	Prohibition of Alcoholic Beverage Advertising.....	24
11.	PROMOTIONAL PROGRAM	
11.1	Promotional Program.....	24
11.2	Promotional Charge	24
12.	WAIVER; INDEMNITY; INSURANCE	
12.1	Waiver.....	25
12.2	Indemnity	25
12.3	Losses.....	25
12.4	Immediate Obligation to Defend.....	25
12.5	Notice.....	25
12.6	Insurance	25
12.7	Form of Policies.....	26
12.8	Delivery of Policies or Certificates.....	26
12.9	Subrogation.....	26

19.9	Federal Affirmative Action Regulations.....	39
19.10	City's Nondiscrimination Ordinance.....	39
19.11	Conflict of Interest.....	40
19.12	Prevailing Rates of Wage.....	40
19.13	Declaration Regarding Airport Private Roads.....	40
19.14	No Relocation Assistance; Waiver of Claims.....	40
19.15	Drug-Free Workplace.....	41
19.16	Compliance with Americans With Disabilities Act.....	41
19.17	Sunshine Ordinance.....	41
19.18	Pesticide Prohibition.....	41
19.19	First Source Hiring Ordinance.....	41
19.20	Labor Peace/Card Check Rule.....	41
19.21	[INTENTIONALLY DELETED]	
19.22	Requiring Minimum Compensation.....	42
19.23	Airport Intellectual Property.....	44
19.24	Requiring Health Benefits for Covered Employees.....	44
19.25	Notification of Limitations on Contributions.....	46
19.26	Food Service Waste Reduction Ordinance.....	46
20.	GENERAL PROVISIONS.....	46
20.1	Notices.....	46
20.2	No Implied Waiver.....	46
20.3	Entire Agreement.....	47
20.4	Amendments.....	47
20.5	Interpretation of Lease.....	47
20.6	Successors and Assigns.....	47
20.7	No Third-Party Beneficiaries.....	47
20.8	No Joint Venture.....	47
20.9	Brokers.....	47
20.10	Severability.....	47
20.11	Governing Law.....	48
20.12	Attorneys' Fees.....	48
20.13	Cumulative Remedies.....	48
20.14	Time of Essence.....	48
20.15	Reservations by City.....	48
20.16	Survival of Indemnities.....	48
20.17	Quiet Enjoyment and Title.....	48
20.18	No Right of Redemption.....	49
20.19	Accord and Satisfaction.....	49
20.20	Joint and Several Liability.....	49
20.21	Estoppel Statements.....	49
20.22	Authority.....	50
20.23	Consents.....	50
20.24	Options Personal.....	50
20.25	Counterparts.....	50